

IN RE: Annual Review of Base Rates for Fuel Costs) ORDER APPROVING
of South Carolina Electric & Gas Company.) BASE RATES FOR
) FUEL COSTS

At the public hearing, Francis P. Mood, Esquire, and Catherine D. Taylor, Esquire, represented SCE&G; Hana Pokorna-Williamson, Esquire, and Elliott F. Elam, Jr., Esquire, represented the Intervenor, the Consumer Advocate for the State of South Carolina (“the Consumer Advocate”); Scott Elliott, Esquire, represented the Intervenor, the South Carolina Energy Users’ Committee (“SCEUC”); and F. David Butler, General Counsel, represented the Commission Staff.

The record before the Commission consists of the testimony of Gene G. Soult, Thomas D. Gatlin, Stephen M. Cunningham (both in Open and Closed sessions), Carl B.

Klein, Gerhard Haimberger, R. Dow Bailey, James W. Neeley, and John R. Hendrix (Direct, Amended Direct, and Rebuttal Testimony) on behalf of SCE&G; the testimony of Jacqueline R. Cherry and A. Randy Watts on behalf of the Commission Staff; and sixteen (16) hearing exhibits, three of which were submitted under seal.

The Commission also has before it a proposed stipulation entered into by and between SCE&G and the Consumer Advocate. This stipulation resulted from Circuit Court appeals of Commission Orders No. 2002-347 and 460 (Docket Number 2002-2-E), and 2003-295 and 387 (Docket Number 2003-2-E). In the appealed cases, the Commission allowed SCE&G to recover the full cost of its economic purchases of electric power, including transportation costs, through the Fuel Clause, so long as the cost of those purchases was less than the Company's avoided costs for the generation of an equivalent amount of power. This method of recovery, supported by the Company, is known as the "avoided cost proxy methodology." By contrast, the Consumer Advocate maintained that the Fuel Clause Statute only permitted the Company to recover its actual costs incurred in purchasing power. However, because of the difficulty often associated with identifying the actual cost of fuel incurred in generating purchased power, the Consumer Advocate urged the Commission to adopt a "cost proxy methodology" as a substitute for the actual cost of fuel where that cost was unknown. The Circuit Court agreed with the Consumer Advocate and remanded the issue to the Commission for disposition. Subsequent to that remand, but prior to our ruling on the issue, the South Carolina General Assembly clarified its intent *vis a vis* the disputed language. The amended Fuel Clause Statute specifically permits the recovery of all costs related to

purchased power utilizing the avoided cost methodology. Thus, pursuant to the Fuel Clause Statute, as amended, so long as SCE&G's economic purchases of electric power are less than the Company's cost of generation for the same amount of power, full recovery of those costs is allowed through the Fuel Clause. Since the rights and obligations under the statute are clear going forward, the proffered stipulation intended to fully and finally resolve the issues left outstanding in Dockets No. 2002-2-E and 2003-2-E. For the reasons discussed herein, the Commission hereby approves both the stipulation and the requested fuel factor.

Based upon the evidence in the record, the Commission makes the following findings of fact and conclusions of law:

FINDINGS OF FACT

1. The record of this proceeding indicates that for the period from March, 2003 through February, 2004, SCE&G's total fuels costs for its electric operations amounted to \$379,801,214. Hearing Exhibit No. 14.

2. Staff reviewed and compiled a percentage generation mix statistic sheet for SCE&G's fossil, nuclear, and hydroelectric plants for March, 2003 through February, 2004. The fossil generation ranged from a high of 92% in November, 2003, to a low of 62% in both March and April, 2003. The nuclear generation ranged from a high of 30% in April, 2003 to a low of 3% in November, 2003. The percentage of generation by hydro ranged from a high of 9% in March of 2003 to a low of 3% in January of 2004. Hearing Exhibit No. 1, Utilities Department Exhibit No. 3.

3. During the March, 2003 through February, 2004 period, coal suppliers delivered 5,584,329 tons of coal. The Commission Staff's audit of SCE&G's actual fuel procurement activities demonstrated that the average monthly received cost of coal (including freight) varied from \$42.00 per ton in April, 2003 to \$46.76 per ton in February 2004. Hearing Exhibit No. 15, Audit Department Exhibits A and C.

4. Staff collected and reviewed certain generation statistics of SCE&G's major plants for the twelve months ending February 29, 2004. The nuclear fueled Summer Plant had the lowest average fuel cost at 0.53 cents per kilowatt-hour. The highest amount of generation was 4,920,946 megawatt-hours produced at the Summer Plant. Hearing Exhibit No. 10, Utilities Department Exhibit 4.

5. The Commission Staff conducted a review and audit of SCE&G's fuel purchasing practices and procedures for the subject period. Based on its audit, Staff adjusted the cumulative under-recovery as of April, 2003 by \$5,432,913. This adjustment consisted of the disallowance of certain purchased power costs in Docket Number 2003-2-E. The Company disagreed with these disallowances, and the Commission did not rule on them in its Order Number 2003-295, but stated that it would await guidance from the courts on the issue. As was stated above, the circuit Court remanded the purchase power issue back to the Commission. However, the Company and the Consumer Advocate have entered into a settlement agreement resolving those issues. Because the Commission, by this Order, accepts that stipulation, the Staff's adjustment is unnecessary. Exhibit 14.

6. The Commission recognizes that the approval of the currently effective methodology for recognition of the Company's fuel costs requires the use of anticipated

or projected costs of fuel. The Commission further recognizes the fact inherent in the utilization of a projected average fuel cost for the establishment of the fuel component in the Company's base rates that variations between the actual costs of fuel and projected cost of fuel would occur during the period and would likely exist at the conclusion of the period. S.C. Code Ann. §58-27-865 (Supp. 2004) establishes a procedure whereby the difference between the base rate fuel charges and the actual fuel costs would be accounted for by booking through deferred fuel expenses with a corresponding debit or credit.

7. In Order No. 2003-295, dated May 1, 2003, the Commission approved a base fuel factor of 1.678 cents per kilowatt-hour, which is currently in effect. Hendrix at 2. Witness Hendrix's projections on behalf of the Company show an actual under recovery of \$20,532,261 at February, 2004 and forecast a total under recovery of \$22,862,377 by April, 2004. Id. For the twelve months May, 2004 through April, 2005, the base fuel cost to the Company is 1.941 cents per KWH, which includes .069 cents per KWH for the anticipated under collection. Id. Witness Hendrix testified that, if the stipulation with the Consumer Advocate is approved, which provides that the outstanding cases would be settled by allowing recovery through the fuel clause of 60% of the disputed costs and deferring 40% for recovery in the Company's next rate case adjusting base electric rates, the Company proposes that the fuel component be set at 1.821 cents per KWH, effective with the billing month of May, 2004, and continuing through the billing month of April, 2005. Id. at 5. We agree with this recommendation for the reasons outlined herein.

8. SCE&G calculated the net capacity factor of the V. C. Summer Station during the review period to be 99.5%, excluding a planned refueling outage and other reductions. Testimony of Gatlin at 2.

CONCLUSIONS OF LAW

1. Pursuant to South Carolina Code Ann. Section 58-27-865(B)(Supp. 2004), each electrical utility must submit to the Commission its estimates of fuel costs for the next twelve (12) months. Following an investigation of these estimates and after a public hearing, the Commission directs each electrical utility “to place in effect in its base rate an amount designed to recover, during the succeeding twelve months, the fuel costs determined by the Commission to be appropriate for that period, adjusted for the over-recovery or under-recovery from the preceding twelve month period.” Id.

2. South Carolina Code Ann. Section 58-27-865(G) requires the Commission to allow electrical utilities to recover “all their prudently incurred fuel costs... in a manner that tends to assure public confidence and minimize abrupt changes in charges to consumers.”

3. As stated by the Supreme Court in Hamm v. South Carolina Public Service Commission, 291 S.C. 178, 352 S.E.2d 476, 478 (1987), Section 58-27-865(F) requires the Commission “to evaluate the conduct of the utility in making the decisions which resulted in the higher fuel costs. If the utility has acted unreasonably, and higher fuel costs are incurred as a result, the utility should not be permitted to pass along the higher fuel costs to its consumers.” “[T]he rule does not require the utility to show that its conduct was free from human error; rather it must show it took reasonable steps to

safeguard against error.” Id. at 478, citing Virginia Electric and Power Co. v. The Division of Consumer Council, 220 Va. 930, 265 S.E.2d 697 (1980).

4. The Commission recognizes that Section 58-27-865(F) provides it with the authority to consider the electrical utility’s reliability of service, its economical generation mix, the generating experience of comparable facilities, and its minimization of the total cost of providing service in determining to disallow the recovery of any fuel costs.

5. Further, S.C. Code Ann. §58-27-865 (F)(Supp. 2002) provides that:

[T]here shall be a rebuttable presumption that an electrical utility made every reasonable effort to minimize cost associated with the operation of its nuclear generation facility or system ...if the utility achieved a net capacity factor of ninety-two and one-half percent or higher during the period under review. The calculation of the net capacity factor shall exclude reasonable outage time associated with reasonable refueling, reasonable maintenance, reasonable repair, and reasonable equipment replacement outages; the reasonable reduced power generation experienced by nuclear units as they approach a refueling outage; the reasonable reduced power generation experienced by nuclear units associated with bringing a unit back to full power after an outage; Nuclear Regulatory Commission required testing outages unless due to the unreasonable acts of the utility; outages found by the [C]ommission not to be within the reasonable control of the utility; and acts of God. The calculation also shall exclude reasonable reduced power operations resulting from the demand for electricity being less than the full power output of the utility’s nuclear generation system. If the net capacity factor is below ninety-two and one-half percent after reflecting the above specified outage time, then the utility shall have the burden of demonstrating the reasonableness of its nuclear operations during the period under review.

6. Upon consideration of the evidence of record, the Commission concludes that SCE&G’s generating facilities, including the new Jasper Facility, were operated

efficiently during the period under review and that the corresponding fuel costs were prudently incurred. This conclusion is based upon the opinion and report of the Staff which indicated that there were no unreasonable Company actions which caused SCE&G's customers to incur higher fuel costs. This conclusion is further supported by the evidence presented by SCE&G that the nuclear unit achieved a net capacity factor as defined in S.C. Code Ann.58-27-865(F) (Supp. 2004) of 99.5%. Additionally, SCE&G's fossil units achieved an availability of 84.19%. By comparison, the NERC five year average of availability of similar sized units from 1998-2002 is 86.71%. Availability was slightly lower than the national average, due to the timing and duration of the normal planned and maintenance shutdown hours associated with equipment maintenance outages and environmental compliance investments. However, during the peak period, June 1, 2003 through September 30, 2003, SCE&G operated at an availability of 94.5%. Testimony of Soult at 4.

The amended and clarified Fuel Clause Statute (updated as of February 2004) addresses the definition of "fuel costs related to purchased power." Section 7(2)(b) of the revised Clause states that the "as delivered" cost of economy power purchases, including transmission (or wheeling) charges may be included in purchased power costs if those costs are "less than the purchasing utility's avoided variable costs for the generation of an equivalent quantity of electric power." Another section of the statute addresses the offsetting of cost of fuel recovered through sales of power to neighboring utilities against fuel costs to be recovered. See Section 58-27-865(E)(Supp. 2004). Section F spells out the rebuttable presumption of prudence in operation by a utility of its nuclear generation

facilities with the attaining of a certain level of production during the review period. Under Section F, costs can be disallowed. The Section shows that the aim of the statute is to encourage the affected utility to operate its production system, including the purchase power option, in the most effective and efficient manner. This is in full concert with the provision of electric service at the most reasonable and prudent rate, through minimization of the total cost of providing service.

In our most recent electric fuel clause cases, the question raised by the testimony and evidence of record has been what is the most appropriate and reasonable proxy to use for purchased power expenses when the corresponding fuel cost is not identified, and, further, should this proxy also be used for interchange transactions, where a fuel cost is listed on the purchase power invoice, but the source of that fuel cost is in question. We are guided in responding to this question, once and for all, by the General Assembly's clarification of S.C. Code Ann. Section 58-27-865. As has been discussed, new Section 7(2)(b) allows an electric utility to recover, as a fuel cost through the electric utility's fuel cost factor, the electric utility's entire purchased power costs incurred during the period under review, provided such purchased power costs are less than the fuel costs the electric utility avoids by making such purchases.

7. After considering the directives of §58-27-865 (B) and (F) which require the Commission to place in effect a base fuel cost which allows the Company to recover its fuel costs for the next twelve months adjusted for the over-recovery or under-recovery from the preceding twelve month period, the Commission has determined that the appropriate base fuel factor for May, 2004 through April, 2005 is 1.821 cents per

kilowatt-hour. The Commission finds that a 1.821 cents per kilowatt-hour fuel component will allow SCE&G to recover its projected fuel costs. The Office of Regulatory Staff shall monitor the cumulative recovery account to assure a proper level of reasonableness.

8. Finally, the Commission also has before it the motion of the Consumer Advocate to open a separate proceeding for the purpose of reviewing SCE&G's prudence with regard to the Jasper Gas Supply contracts. Subsequent to this hearing, but prior to our written order in this matter, the Commission did, in fact, undertake such a review in Docket Number 2004-126-E. We, therefore, confine our discussion of the Jasper Gas Supply contracts to that docket, and restrict our findings here to the fact that the Jasper Plant, as all other SCE&G plants reviewed in this docket, was operated prudently.

IT IS THEREFORE ORDERED THAT:

1. The base fuel factor for the period May, 2004 through April, 2005 is set at 1.821 cents per kilowatt-hour.
2. The stipulation between SCE&G and the Consumer Advocate is hereby accepted, making Staff's requested downward adjustment unnecessary.
3. SCE&G shall file an original and ten (10) copies of the South Carolina Retail Adjustment for Fuel Cost Tariff within ten (10) days of receipt of this Order.
3. SCE&G shall comply with the notice requirements set forth in S.C. Code Ann., §58-27-865 (B) (Supp. 2004).
4. SCE&G shall continue to file the monthly reports as previously required.

5. SCE&G shall account monthly to the Commission for the differences between the recovery of fuel costs through base rates and the actual fuel costs experienced by booking the difference to unbilled revenues with a corresponding deferred debit or credit. The Office of Regulatory Staff shall monitor the cumulative recovery account.

6. SCE&G shall submit monthly reports to the Commission and the Office of Regulatory Staff of fuel costs and scheduled and unscheduled outages of generating units with a capacity of 100 MW or greater.

7. This Order shall remain in full force and effect until further order of the Commission.

BY ORDER OF THE COMMISSION:

/s/
Randy Mitchell, Chairman

ATTEST:

/s/
G. O'Neal Hamilton, Vice Chairman

(SEAL)